

The IRS Provides Much Needed Relief Procedures for S Corporation Elections

November 4, 2022



The S Corporation tends to be the most popular option when selecting a corporation status for small businesses, as one of the biggest benefits of this structure is the ability to avoid the double taxation that exists with a C Corporation. However, making and maintaining a valid S Corporation election can be difficult and significant issues can arise for the shareholders.

If the IRS successfully challenges an entity's S Corporation status, the entity automatically reverts to C Corporation status, which could give rise to significant unexpected federal income tax consequences. To mitigate this unanticipated exposure previously, a taxpayer's only relief was to file a private letter ruling (PLR) seeking approval to maintain its S Corporation status.

The good news is that the IRS recently issued guidance under Revenue Procedure 2022-19, providing a series of "taxpayer assistance procedures" to resolve certain issues involving S Corporations and their shareholders to maintain S Corporation status without requiring the issuance of a PLR.

The goal of the guidance is to reduce the burdens on taxpayers, facilitate increased

compliance with S Corporation election rules, and reduce costs and delays that may occur when completing transactions involving S Corporations, such as the sale of the business.

The areas of relief covered by this IRS guidance include the following:

- One class of stock requirement and governing provisions, including “principal purpose” conditions. The IRS will not treat an S Corporation as violating the one class of stock requirement as a result of an agreement that does not have a principal purpose to circumvent the one class of stock requirement.
- Disproportionate distributions when typically all S Corporation shareholder distributions must be pro-rata.
- Some inadvertent errors or omissions on the S Corporation election, Form 2553.
- Missing administrative acceptance letters for an S election (may need the S Corporation election acceptance letter as part of due diligence when selling a company).
- Federal income tax return filings inconsistent with an S Corporation election.
- Corrective relief procedures to allow taxpayers in some situations to retroactively preserve S elections that are invalid or terminated solely because of certain “non-identical governing provisions” which result in the S corporation having more than one class of stock and, therefore, potentially losing its eligibility to remain an S corporation.

For more information on these newly issued relief procedures for S Corporation elections and to determine whether they may provide assistance in maintaining your organization’s entity status, please contact Tax Partner [Alek Dziedzic](#) or your Anchin Relationship Partner.